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In the Supreme Court of the United States

OCTOBER TERM, 1965

HARRY B. SMITH AND MARY L. SMITH, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the district court is reported at 192 F. Supp. 208. The opinion of the court of appeals (Pet. 26–30) is reported at 304 F. 2d 267.

JURISDICTION

The judgment of the court of appeals was entered on June 13, 1962. The petition for a writ of certiorari was filed on August 29, 1962. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

QUESTION PRESENTED

Whether, assuming (without conceding) that Section 117(q) of the 1939 Code set in motion a new limitations period commencing on the date of its enactment, June 29, 1956, taxpayer's suit is nonethe-

less barred by his failure to file a claim for refund within two years thereafter, as required by Section 322(b)-(1) of the 1939 Code and Section 7422(a) of the 1954 Code.

STATUTES INVOLVED

Internal Revenue Code of 1939:

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * * *

(q) [as added by Sec. 1, Act of June 29, 1956, c. 464, 70 Stat. 404] *Transfer of Patent Rights.*—

(1) *General Rule.*—A transfer (other than by gift, inheritance, or devise) of property consisting of all substantial rights to a patent, or an undivided interest therein which includes a part of all such rights, by any holder shall be considered the sale or exchange of a capital asset held for more than 6 months, regardless of whether or not payments in consideration of such transfer are—

(A) payable periodically over a period generally coterminous with the transferee's use of the patent, or

(B) contingent on the productivity, use, or disposition of the property transferred.

* * * * *

(4) *Applicability.*—This subsection shall apply with respect to any amount received, or payment made, pursuant to a transfer described in paragraph (1) in any taxable year beginning after May 31, 1950, regardless of the taxable year in which such transfer occurred.

SEC. 322. REFUNDS AND CREDITS.

[as amended by Sec. 172(e), Revenue Act of 1942, c. 619, 56 Stat. 798.]

(a) *Authorization.*—

(1) *Overpayment.*—Where there has been an overpayment of any tax imposed by this chapter, the amount of such overpayment shall be credited against any income, war-profits, or excess-profits tax or installment thereof then due from the taxpayer, and any balance shall be refunded immediately to the taxpayer.

* * * * * *

(b) *Limitation on Allowance.*—

(1) *Period of limitation.*—Unless a claim for credit or refund is filed by the taxpayer within three years from the time the return was filed by the taxpayer or within two years from the time the tax was paid, no credit or refund shall be allowed or made after the expiration of whichever of such periods expires the later. If no return is filed by the taxpayer, then no credit or refund shall be allowed or made after two years from the time the tax was paid, unless before the expiration of such period a claim therefor is filed by the taxpayer.

* * * * * *

Internal Revenue Code of 1954:

SEC. 7422. CIVIL ACTIONS FOR REFUND.

(a) *No Suit Prior to Filing Claim for Refund.*—No suit or proceeding shall be main-

tained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Secretary or his delegate, according to the provisions of law in that regard, and the regulations of the Secretary or his delegate established in pursuance thereof.

* * * * *

28 U.S.C.:

SEC. 2401. TIME FOR COMMENCING ACTION AGAINST UNITED STATES.

(a) Every civil action commenced against the United States shall be barred unless the complaint is filed within six years after the right of action first accrues. The action of any person under legal disability or beyond the seas at the time the claim accrues may be commenced within three years after the disability ceases.

* * * * *

STATEMENT

The stipulated facts (R. 9a–13a),[1] some of which were found by the district court (R. 13a–18a), may be summarized as follows:

Taxpayer, Harry B. Smith, and George A. Dolan were co-inventors and co-owners of two devices,

[1] Record references are to the separately printed Appendix to the government's brief in the court of appeals.

described as "Pipe Welding and Heat Treating Process" and "Means for Heat Treating and Welding Metal Parts." A patent on the former device was issued to the inventors on December 26, 1939, and an application for letters patent on the latter invention was executed by Smith and Dolan on December 18, 1946. (R. 10a.) Pursuant to an agreement executed on January 20, 1947, Smith and Dolan, as licensors, granted an exclusive license to these devices to Electric Arc, Inc., a New Jersey corporation. Under the terms of the agreement, the grantors were to receive royalties based upon a percentage of the net sales price received for any electric heating apparatus or appliance manufactured, sold or rented by the licensee. Neither Smith nor Dolan were ever employed by, or owned stock in, Electric Arc, Inc. (R. 10a–12a.)

In addition to the patents mentioned in the 1947 agreement, Smith had obtained patents on two other devices: "water catcher" and a "gasketless joint." (R. 12a.) Smith was regularly employed from 1929 through 1957 by United Engineers and Constructors, Inc., rising from master mechanic to vice-president and construction manager. From 1920 to 1929, he had been employed as a master mechanic by a corporate subsidiary of United Engineers. (R. 9a–10a.)

During 1951 and 1952, Smith received royalties under the 1947 agreement in the respective amounts of $19,784.12 and $37,075.43. These amounts were reported by taxpayers[2] as ordinary income for those

[2] Mary L. Smith is a party to this action solely because of the filing of joint returns during the years in issue.

years on joint income tax returns that were timely filed. (R. 11a–13a.)

The transfer of patent rights effected by the 1947 agreement fell within the class of transfers described in Section 117(q) of the Internal Revenue Code of 1939, which was enacted by Section 1 of the Act of June 29, 1956, c. 464, 70 Stat. 404. (R. 11a, 13a–14a.) On July 15, 1958, taxpayers filed claims for refund of the income taxes paid for 1951 and 1952, on the ground that the proceeds received under the 1947 agreement were properly reportable as long-term capital gains, and not ordinary income. No administrative action having been taken on these claims within six months after they were filed, the taxpayers, on February 20, 1959, instituted suit for recovery of the taxes in question. (R. 11a–12a.)

In defense, the United States contended that since taxpayers had failed to file refund claims within the time prescribed by the limitations provisions set forth in Section 322(b)(1) of the 1939 Code, the district court, under Section 7422(a) of the 1954 Code, was without jurisdiction to hear the matter. (R. 12a, 14a.) Nevertheless, the district court entered judgment for the taxpayers. (R. 18a.) On appeal by the United States, the court below reversed. (Pet. 30.)

ARGUMENT

The decision below is correct, is not in conflict with any other decision, and presents no question warranting review by this Court.

1. Under the provisions of Section 117(q)(4), *supra*, p. 2, the relief afforded by that section is made ap-

plicable to taxable years beginning after May 31, 1950. However, Section 322(b)(1), *supra*, p. 3, states that unless a claim for refund is filed within three years from the time taxpayer filed his return, or two years from the time the tax was paid, no refund shall be allowed. Since taxpayer's refund claims for the taxes paid for 1951 and 1952 were not filed until July 15, 1958, the United States contended below that the suit was barred by these limitations provisions and by Section 7422(a), *supra*, p. 3.

In *Zacks* v. *United States*, 280 F. 2d 829 and *Lorenz* v. *United States*, 296 F. 2d 746, the Court of Claims held that the enactment of Section 117(q) on June 29, 1956, created a new cause of action and set in motion a new limitations period. This result is in conflict with that reached in *Tobin* v. *United States*, 264 F. 2d 845 (C.A. 5) and *United States* v. *Dempster*, 265 F. 2d 666 (C.A. 6), certiorari denied, 361 U.S. 819, which held that the 1956 Act did not reopen years already barred by Section 322(b)(1) and Section 7422(a). The government strongly disagrees with the conclusion of the Court of Claims and, simultaneously with this brief, is filing a petition for a writ of certiorari in *Zacks*.

2. In the case at bar, even if the *Zacks* rule were followed, petitioner's claim would still be barred by the statute of limitations, as the court below held. The Court of Claims decisions holding that the Act of June 29, 1956, created a new cause of action also subscribe to the theory that it gave rise to a constructive overpayment of tax as of the date the

Act was approved[3] and that the appropriate limitations period to be computed from that date is therefore the two year period which, under Section 322(b)(1), runs "from the time the tax was paid." Since the taxpayers here did not file claims for refund until July 15, 1958, more than two years after the enactment of Section 117(q), their suits would be barred even under the decisions most favorable to them.

If it be assumed that the enactment of a retroactive tax relief measure has the effect of creating by implication a new limitations period—a proposition we strenuously deny—the further question whether that period should be two years (on the theory of a constructive overpayment of tax) or, as petitioners urge, three years (on the theory that it "expires the later") or six years (as contemplated by 28 U.S.C. 2401, on the theory of an implied repealer of Section 322(b)(1)) is not a matter of basic principle warranting review by this Court in the absence of a conflict. The two-year period is, we think, a more plausible choice

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[3] See *Eastman Kodak Co.* v. *United States*, 292 F. 2d 901, 904, 905 (Ct. Cls.); *Lorenz* v. *United States*, 296 F. 2d 746. In an unreported decision, *Walter* v. *United States*, C. Cls. No. 160-62, the Court of Claims held that a claim filed more than two years after the enactment of Section 117(q) was untimely. Following this decision, four similar cases pending in the Court of Claims were dismissed either by order or stipulation. *Allandre* v. *United States*, C. Cls. No. 209-62 (Stipulation dated September 28, 1962); *Church* v. *United States*, C. Cls. No. 205-62 (order dated October 22, 1962); *Caster* v. *United States*, C. Cls. No. 469-60 (order dated October 22, 1962); *Puschelberg* v. *United States*, C. Cls. No. 194-60 (order dated November 2, 1962).

than either of the alternatives. In any event, however, since that period has been adopted by the only two courts which have considered the matter, taxpayers are now amply forewarned that they must file their refund claims within two years. It seems extremely unlikely that any future court will be disposed to reject these precedents and throw the issue into confusion.

CONCLUSION

For the reasons given, we respectfully submit that the petition for a writ of certiorari should be denied.

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